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SUBJECT: IMF REPORTS PROGRESS AND PROBLEMS FOR ZIM
MACROECONOMY

¶1. (SBU) SUMMARY: During an October 13 briefing for OECD Ambassadors in Harare, IMF Mission Chief Vitaly Kramenko reported that progress in budgetary execution was encouraging, but that problems remained, including concerns about the Reserve Bank of Zimbabwe (RBZ), wages and rule of law. He said the IMF would not pursue a staff monitored program unless donors were committed to providing a debt treatment for Zimbabwe. The EU reported its dialog with the GOZ was stalled and the World Bank had no progress to report on the programmatic Multi Donor Trust Fund (MDTF). Apart from the Ministry of Finance, there are few bright spots on the economic horizon. END SUMMARY.

IMF SEES PROGRESS

¶2. (SBU) An IMF team led by Vitaly Kramenko provided an in-brief to OECD Heads of Mission on October 13; the team expressed willingness to provide an outbrief on October 26, perhaps to include a teleconference with the like-minded donor meeting in Berlin. They reported that the Finance Ministry had maintained close contact with the IMF since the team's last Mission in March, and they thought they had a solid understanding of fiscal developments. On that basis, they believed that Zimbabwe had made significant progress. The multi-currency system was generally working, and the IMF stood ready to provide advice on how the GOZ might adapt it upon selecting an anchor currency. Cash budgeting was successful, and the Zimbabwe Revenue Authority (ZIMRA) was doing well, following implementation in the revised budget of IMF recommendations on tax policy. Service delivery, though still far from optimal, had improved, with schools and hospitals open.

BUT ALSO MAJOR CONCERNS

13. (SBU) Despite this progress, the IMF saw three major problems threatening economic recovery in Zimbabwe. First, Kramenko said that the IMF had received no data since March from the RBZ, and had concerns relating to the Bank. There was no solid foundation for improved RBZ governance; the Reserve Bank Act did not follow the IMF's recommendations, and the IMF believed that Biti had been forced to make significant concessions as the Act progressed through the Cabinet. As it stands, the Act does not establish an institutional setting with appropriate checks and balances, but instead relies on personalities. Kramenko said the payment system was just starting to operate in the multicurrency environment, and lack of confidence in Governor Gono created vulnerabilities. A rumor recently circulated among members of the donor community that Gono had misappropriated commercial banks' statutory reserves lodged at the RBZ. Kramenko noted that the IMF had no evidence that the RBZ was holding counterpart funds and thus the rumor could be true. If reserves proved unavailable when required, confidence would be destroyed and economic recovery would suffer a severe setback. (NOTE: Local bankers, who have a strong vested interest in the matter, have told Econoff they are confident the RBZ has not misused their reserves. END NOTE.)

14. (SBU) Kramenko also expressed concern about civil service wage increases. He said they threatened the economic recovery in two respects. First, they undermined private sector competitiveness. Without a national currency, devaluation to restore competitiveness is not an option, so

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this effect will endure. Second, they eliminated fiscal space for infrastructure investment. This ultimately undermines both service delivery and competitiveness.

15. (SBU) The IMF's third issue of concern was rule of law and property rights. Kramenko noted that continuing farm invasions had a clear effect on investment climate, especially for agriculture. In addition, uncertainty about implementation of indigenization requirements affected other sectors, including the mining sector.

NEXT STEP DEPENDS ON DONORS

16. (SBU) Kramenko told the Heads of Mission that the IMF would not move forward to establish a staff monitored program (SMP) for Zimbabwe in the absence of donor commitment to support a debt treatment. While there was no guarantee an SMP would succeed in any case, there was no point in implementing one without an incentive for good performance.

EU, WORLD BANK REPORT ON DEVELOPMENTS

17. (SBU) The Swedish Ambassador told the group that the GOZ - EU dialog (which has the potential to restore GOZ access to direct EU financial support) is languishing. The GOZ has assigned negotiating responsibility to a team of six permanent secretaries. The permanent secretaries are long time functionaries with reactionary habits and likely ZANU-PF sympathies. They appear to have neither the inclination nor the authority to engage in serious discussions about rule of law and protection of property rights. The EU has told Prime Minister Tsvangirai and MDC-M Minister of Regional Integration and International Cooperation Misihairabwi-Mushonga that the effort is stalled, and is waiting to see if they do something about it.

18. (SBU) World Bank representative Mungai Lenneiye reported on the programmatic MDTF. (NOTE: The analytical MDTF, to which the USG provided a contribution, is operational. END NOTE.) He said the Bank board had approved the MDTF and

authorized \$1 million, but donors had not yet contributed because they remained concerned about the administrative rules for operation of the MDTF. The Bank thought that the MDTF Operational Manual should include the possibility of direct funding to government in the future, even though for the time being concerns about public sector financial management precluded budget support. Donors disagreed. A visiting World Bank infrastructure expert from Mozambique chimed in to lecture donors about the wisdom of following the World Bank lead on such matters, noting that the Bank had the highest fiduciary standards and would never make a misstep since it had to answer to its Board.

¶9. (SBU) Donors also briefed the IMF team on the pending civil service and land audits. The civil service audit was stalled because the GOZ refused to include the security services. The land audit was similarly stalled because of Qservices. The land audit was similarly stalled because of GOZ restrictions on scope. In both cases, funding was available.

¶10. (SBU) COMMENT: Biti's relative success at the Ministry of Finance remains an isolated, if important, development. Zimbabwe's economic stabilization is laudable, but progress from stabilization to recovery will remain glacial until decision-makers exercise the political will to move forward

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on rule of law and protection of property rights. It remains evident that RBZ Governor Gono has the ability to undermine confidence singlehandedly, and his further marginalization, if not removal, is much to be desired. END COMMENT.

PETTERSON